American Insurance Association

STATEMENT OF ALASTAIR SHORE
ON BEHALF OF THE
AMERICAN INSURANCE ASSOCIATION
AND THE
AMERICAN COUNCIL OF LIFE INSURERS

BEFORE THE

SUBCOMMITTEE ON CAPITAL MARKETS, INSURANCE AND GOVERNMENT SPONSORED ENTERPRISES

COMMITTEE ON FINANCIALSERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

HEARING ON

"EXAMINING PROPOSALS ON INSURANCE REGULATORY REFORM"

APRIL 16, 2008

Good afternoon. My name is Alastair Shore, and I am the Chief Underwriter of CUNA Mutual Group. CUNA Mutual Group is the leading provider of financial services to credit unions and their members worldwide, offering lending, protection, financial, employee and member solutions through strategic partnerships, technological innovations and multiple service channels. The mutual insurers of the CUNA Mutual Group are owned by their policyholders and operate to serve their best interests.

The pioneers of the credit union movement established the CUNA Mutual Insurance Society in 1935. It is the parent organization of all companies that together form the CUNA Mutual Group. In 2007, we paid out more than $1.4 billion in claims and generated $3.1 billion in revenue. We also managed $7.17 billion in assets for third-party clients, including member investments, credit union employee pension assets, and credit union assets.

I am here to testify today on behalf of CUNA Mutual Group and our insurance trade associations, the American Insurance Association (AIA) and the American Council of Life Insurers (ACLI). Like the other members of our trade associations, CUNA Mutual Group strongly supports Optional Federal Chartering (OFC) for insurance companies as the best alternative for modernizing and reforming the current state-based insurance regulatory system. We appreciate the opportunity to testify at today's hearing examining OFC and other proposals on insurance regulatory reform. And, I would like to thank the Subcommittee for the leadership it has taken in understanding the need for insurance regulatory reform and its commitment to finding the best solution.

We sincerely believe this analysis will lead the Subcommittee inescapably to OFC—a system that will provide a single regulatory authority for insurers that choose to be regulated at the federal level, while keeping the state-based regulatory system in place for companies that choose to remain state-regulated. An OFC, as set forth in the National Insurance Act of 2007 (H.R. 3200 or NIA), represents our best opportunity to advance regulatory modernization in a manner that works for consumers, the industry, and the economy.

At its core, the NIA is a strong consumer protection bill, which focuses on a robust centralized system that emphasizes safety, soundness and consistent market conduct regulation. These consumer protections are reinforced through separate consumer affairs and insurance fraud divisions and a new federal ombudsman. Together, these regulatory powers will create a presence that can more quickly respond to consumers than the current, fragmented state regulatory system.

The issue of insurance regulation, once thought to be the province of isolated industry practitioners and regulators, is now central to many of the critical public policy debates over the direction of the financial services sector and the U.S. economy. Insurance regulation, specifically OFC, is featured prominently in the Treasury Department’s recently released Blueprint for a Modernized Financial Regulatory System. As you know, the Treasury Blueprint recommends the establishment of a federal insurance regulatory structure to provide for the creation of an OFC system. We strongly support Treasury’s view that an OFC would play an important role in the new world of integrated and interconnected financial markets, and would address the increasing cost and efficiency burdens that our disjointed state insurance regulatory system imposes on insurers and consumers alike.

The Treasury blueprint also recognizes the important role that the insurance industry now plays in our new financial world. Insurers, banks and capital market investors (which in the past operated in largely separate markets) are now offering products that may be substitutes for each other, and there also is a trend toward one-stop shopping for finance and risk management needs. Insurers must have a regulatory system that adapts to market realities and allows them to compete on a level playing field and to serve the evolving needs of their policyholders.

Moreover, the turmoil that has recently roiled the financial services sectors highlights the interconnectedness of our financial system and the importance of insurance to the proper functioning of that system. This is precisely the time to enact regulatory reforms that strengthen solvency oversight and foster a more competitive regulatory environment for insurers at the federal level. Waiting will make it more difficult to correct existing problems and runs the risk that policyholders may suffer in time of loss.

An OFC will greatly improve insurers' ability to provide essential financial protection to the millions of policyholders who rely on insurance payments when faced with loss. Insurance helps individuals and businesses to assume the risks that are inevitable in life and business, with the security of a strong financial safety net in place when loss occurs. Without insurance, and a sound regulatory structure to promote its benefits, societal innovations and advancement become more risky and less likely to become reality.

The Critical Need for Insurance Regulatory Reform

The current state insurance regulatory system basically reflects a system that began in the 19^{th} century and continued to grow as a result of the McCarran-Ferguson Act. That law was enacted in 1945 largely to deal with federal antitrust and state tax concerns arising from a 1944 U.S. Supreme Court determination that insurance was a product in interstate commerce and, therefore, subject to federal authority.

McCarran is a power-sharing statute that reflects Congress' considered judgment to delegate – *not abdicate* – its authority over insurance to states that regulate the business of insurance themselves. In doing so, McCarran recognizes that Congress has the right to intervene in insurance regulatory matters by enacting specific federal laws.

Under McCarran, the states have put in place sweeping and stifling regulatory regimes that dictate what products insurers can provide, how much they can charge for these products, and how they conduct even the most routine aspects of their business. The result has been a regulatory scheme that: 1) is lacking uniformity or efficiency for insurers or their customers; 2) reflects assumptions about the insurance industry and its consumers that are grounded in the 19^{th} century and are far from accurate today; and 3) is unduly focused on government intrusion in the market, particularly in the area of insurance rate and form oversight.

It has been apparent for a long time that the current state insurance regulatory system is costly and inefficient with respect to time lost and money spent to comply with a patchwork of antiquated and inconsistent state requirements. Ultimately, the consumer pays for this inefficiency through higher costs, reduced product offerings, and less consumer choice. An OFC system can provide strong, centralized financial oversight and consumer protection regulations and examinations that are tailored to real problems facing consumers with respect to consumer education, policy disclosures, claims, and other issues.

Additionally, the unwieldy regulatory system is contributing to the outflow of risk-bearing capital from the U.S. to jurisdictions with more rational, predictable and efficient regulatory systems. This does not bode well for the long-term health of the country's domestic insurance industry. According to two major reports on global competitiveness in the financial services industry (Schumer/Bloomberg and the U.S. Chamber), U.S. insurers wishing to operate on the world stage are hampered by restrictive regulation that their foreign competitors do not face. As a result, the flow of new capital in the insurance industry is moving in one direction—away from the U.S. Virtually all of the new capital that is now securing U.S. risks is domiciled in jurisdictions that provide more centralized, efficient and uniform regulatory systems. OFC would allow the new capital providers (and all U.S. insurers) with a choice of a centralized regulatory system that permits them to remain onshore, thus enhancing, rather than impairing, the competitiveness of the U.S. insurance industry in our global economy. Creating such a system for insurers would mirror the one that has been in place for the banks and credit unions, and which has overall served both the nation's citizens and economy very well.

Moreover, the choices facing capital providers will become further restricted as our international trading partners move to develop more streamlined insurance regulatory models that threaten to leave the U.S. even farther behind. One such development involves the introduction of risk-based insurer solvency requirements across the European Union, through an initiative that is known as “Solvency II.” The new solvency requirements will be more risk-sensitive and more sophisticated than in the past, thus enabling better tracking of the real risks run by any particular insurer, while at the same time encouraging competition and innovation. As a result, trade experts believe that Solvency II will enhance the international competitiveness of EU insurers to the detriment of their U.S. peers. U.S. insurers cannot be easily integrated into Solvency II because the U.S. does not provide supervision equivalent to that of the EU. Because it is merely a committee of well-intentioned, individual state supervisors and not a national regulatory body that can guarantee uniformity and consistency, the NAIC cannot adequately address this situation. As noted in a recent analysis of Solvency II by Standard and Poors, “in the absence of supervisory equivalence, non-EU insurers may find themselves operating at a competitive disadvantage in Europe.” U.S. insurers are also concerned that the growing cohesiveness of the EU under Solvency II will yield cost and efficiency benefits for EU insurers that cannot be realized under the highly fragmented state system in the U.S.

A Better Regulatory Alternative

For these reasons, we strongly support the National Insurance Act of 2007 (H.R. 3200), introduced last July by Reps. Melissa Bean (D-IL) and Ed Royce (R-CA), along with its Senate counterpart (S. 40). For national companies, an optional federal charter would displace the current multi-state patchwork regulatory system with a framework for uniformity, consistency, and clarity of regulation that is focused on consumer needs and protection.

We need a new regulatory alternative based on a rational and efficient reallocation of regulatory resources to focus uniformly on the most critical aspects of the insurance safety net and consumer protections, and not on regulatory red tape and government decisions concerning the "appropriate" rate for an insurer to charge or the "appropriate" insurance policy to offer to consumers. The new system must replace the current conflicting state requirements with regulatory uniformity for insurers operating at the multi-state or national level. H.R. 3200 embodies all of the elements of this paradigm and represents the best approach for Congress to move forward in advancing reform.

H.R 3200 does not regulate prices charged or products offered by market participants, because it recognizes that governments, acting unilaterally in these areas, cannot be effective surrogates for the free market. As noted in the Treasury report, "while numerous arguments have been made to justify rate regulation, they are unpersuasive." States that do not impose onerous regulatory controls enjoy vigorous competition, healthy markets, and stable overall rates. According to a recent ConsumerGram published by the American Consumer Institute, consumers living in states with high levels of insurance regulation pay hundreds of dollars more per year than consumers living in states with less insurance regulation.

Although H.R. 3200 effectuates a fundamental shift in regulatory application, it also proposes to put in place a regulatory oversight regime as strong, or stronger, than any found in an individual state today. Contrary to what detractors will offer, it does not preempt state premium tax regimes or abandon aspects of the state system that are necessary for consumer protection. It also recognizes that there will always be a need for markets of last resort – so-called "residual markets" – and that national insurers must participate in those markets mandated by state law.

To bolster the consumer approach of OFC, H.R. 3200 establishes stronger, re-focused regulation in those areas where regulation is necessary to protect consumers as they both navigate the marketplace and turn to insurers for payment of covered claims. Above all, enactment of H.R. 3200 will assure that insurance company solvency remains strong despite the ever-changing nature of risk. The Act also establishes both a federal ombudsman to serve as a liaison between the federal regulator and those affected by the regulator's actions, as well as consumer affairs and insurance fraud divisions to provide strong consumer service and protection.

Over the long-term, it is our view that a federal regulatory option, structured in the way set forth in H.R. 3200, will modernize regulation of the industry, empowering consumers and emphasizing market conduct and financial solvency oversight in the process. In creating these needed systemic reforms, the Act will consolidate regulation into a single uniform point of enforcement for those that choose the federal charter, without forcing change for those remaining in the state system.

The Critical Need to Move Forward

Insurance regulatory reform is a critical imperative that will determine the long-term viability of one of our nation's most vital economic sectors, and help define how our economy manages risk in the future. The choice is between the existing state regulatory bureaucracy grounded in the 19th century or a new approach that relies on individual choice, competition, and the evolution of our customers' needs in a 21st century global economy.

As the committee considers reform of the current system, we believe that the three basic principles that define the optional federal charter approach in H.R. 3200 must be followed:

- ✓ establish uniform, consistent, and efficient regulation; and
- ✓focus regulation on those areas where government oversight protects consumers in the marketplace, such as financial integrity and market conduct, rather than on those activities that distort the market, such as government price controls and hostility to innovation; and
- ✓place primacy on the private market, not regulatory fiat, creating an environment that empowers consumers as marketplace actors.

Creating an optional federal charter is imperative to meet the needs of customers and insurers alike. We appreciate the Subcommittee's interest in this important subject and look forward to working with the Subcommittee to improve our nation's insurance regulatory system.